Contents

Questions within the Workbook should be treated as preparation questions, providing you with a firm foundation before you attempt the exam-standard questions. The exam-standard questions are found in the Question Bank.

Chapter 1

The macro environment

Introduction

Learning outcome

- Analyse for a given situation the external factors which may impact upon an organisation's performance and position, identifying significant issues in areas such as:
  - Sustainability, including natural capital and climate change
  - Macroeconomic forces
  - International trade, financial systems and global economic factors
  - Government policies
  - Its industry and markets, including competition
  - Cultural environment
  - Stakeholder impact
  - Markets for finance, labour and other resources
  - Supply chain factors
  - Technology developments, including those relating to automation and intelligent systems

Specific syllabus reference for this chapter is: 1b.

Syllabus links

Environmental analysis was covered in Business, Technology and Finance. However its coverage was at the level of core knowledge. In the Business Strategy and Technology examination you will be required to apply it.

Examination context

The scenarios in the majority of exam questions will require you to absorb and understand information about the external environment in which an organisation operates, based on a scenario. You will also need to assess the implications of the environment and changes in the environment for the strategic positioning and strategic decisions of an organisation. To do this you will need to apply your knowledge using the tools and ideas covered in this chapter.

Q3 in the September 2018 exam (*Vision Bank*) focused on a small, traditional bank. In response to technological change in the banking industry, Vision Bank (VB) wanted to launch a banking app and implement a new, digital-only banking strategy. This strategy would involve shutting down its processing centre which produced paper bank statements.

The first requirement asked candidates to:

'Prepare a report for VB's board which identifies and analyses **three** key external factors that are creating change in the European banking industry. Refer to relevant models. **(10 marks)**

In requirements such as this where the model(s) to use are not specified, you will need to use your judgement and select the model or framework that you think will add the most value to your answer. Having studied the learning materials, the mention of 'relevant models' in the context of external factors should provide a clear indication that the use of the PESTEL framework (discussed in this chapter) and/or Porter's five forces model (discussed in the chapter The industry and market environment) would be most appropriate.

As well as applying relevant models, it is particularly important that candidates recognised that they were only asked to analyse three key factors. Determining which factors can be considered most important requires judgement. However, careful reading of the question scenario should help to identify the main issues.

The examiner highlighted that the higher scoring answers linked the use of models, where more than one model was used; for example, how new legislation in the banking industry (legal factors in the PESTEL model) was helping to reduce barriers to entry, which is part of Porter's five forces.

Applying a theoretical model or framework in its entirety, or discussing the model in general terms, when not asked to do so will only serve to waste your time in the exam, and will earn no additional marks.

In light of the name of the exam, Business Strategy and Technology, it is important that you appreciate the impact that technology and technological change is having on organisations. Exam questions could easily feature organisations which are dependent on the use of technology in delivering a service or as part of the process for new product development. Clearly, in such cases, technology will be vital to the organisation's ability to operate effectively.

Q1 in the March 2017 exam (*Ignite plc*) focused on a company which manufactured luxury cigarette lighters, and other types of products. It was set up when smoking was fashionable but had subsequently experienced declining sales as smoking became unpopular, with many people having switched to e-cigarettes. The first requirement asked candidates to:

'Analyse the external factors that influenced the changing demand for Ignite's cigarette lighters in the UK between 1950 and 2016.'
(9 marks)

Although, no specific model was requested in the requirement the level of detail outlined in the scenario regarding changes in social attitudes, government legislation and technological developments provided a strong clue that use of the PESTEL model was highly appropriate.

Chapter study guidance

Use this schedule and your study timetable to plan the dates on which you will complete your study of this chapter.

Topic	Practical significance	Study approach	Exam approach	Interactive questions
1	**The business environment** The development of emerging economies, the fast pace of technology and the increasing demands of consumers all bring new markets and new challenges. If an organisation is to survive, these factors must be addressed and managed via appropriate strategy development.	**Approach** Read through this section to gain an understanding of the general macro-environment. **Stop and think** What are the main factors, stemming from the macro-environment, that an organisation needs to manage?	This chapter introduces the wider business environment. There is no need to memorise all the examples but rather try to appreciate the range of issues (including technological considerations) influencing organisational behaviour and strategy.	**IQ1: Considering the business environment** This application activity asks you to consider the external influences affecting a professional accountancy practice.
2	**Environmental dynamics** Strategy planning occurs in an uncertain environment so the development process and the strategy itself need to be flexible enough to deal with this uncertainty.	**Approach** Understand the nature of uncertainty presented by the external environment and the process by which an organisation can manage this uncertainty.	You may be required to recommend how an organisation can reduce uncertainty in a dynamic environment. Recommendations should be practical and appropriate to the size and scale of the organisation in the question.	

Topic	Practical significance	Study approach	Exam approach	Interactive questions
		Stop and think In what circumstances is scenario planning neither helpful nor appropriate in managing uncertainty?		
3	**PESTEL analysis** The macro-environment exposes an organisation to a wide range of risks. To comprehensively assess these risks, models such as the PESTEL framework can be used.	**Approach** Read through the examples given for each of the headings in the PESTEL framework. There is no need to memorise these examples but you should appreciate the range of issues that a company can face. **Stop and think** What would be the main risks facing the organisation you work for, using the PESTEL framework to generate ideas?	In the majority of exam questions, you will be required to absorb and understand information about an organisation's external environment, based on a scenario. You will also need to assess the implications of changes in the environment for the strategic positioning and strategic decisions of an organisation. To do this you will need to apply your knowledge using tools such as PESTEL.	**IQ2: Estate agent industry** This question contains a comprehensive scenario to which you need to apply the PESTEL framework. Rather than simply stating the factors that affect the estate agent industry, you need to explain their impact and influence.
4	**The international business context** The majority of businesses are exposed to global influences, whether in their supply chain, via customers, or through the regulations they adhere to. Globalisation requires a strategic response from organisations.	**Approach** Read through the section to understand the importance of globalisation in general terms. The Five C's model (Ohmae) and Michael Porter's Diamond are key theories to help understand the interactions of organisations in a global environment. **Stop and think** Consider the degree of globalisation of your firm. What impact does this	The models in this chapter will be used to assess why an organisation might act globally or what national competitive advantage they may hold. As always, just restating models or theory is not sufficient to be awarded marks, instead they must applied to the scenario provided.	**IQ4: Why do banks cluster?** This short question helps you to understand the concept of clustering, put forward by Michael Porter, by looking at a real-life industry.

Topic	Practical significance	Study approach	Exam approach	Interactive questions
		have on your own work?		
5	**Limits to globalisation of business** In reality, trade between countries is often hindered by rules, regulations and political directives. This topic reviews the types protectionist measures in place globally and the impact of these on organisations and their competitive position.	**Approach** Work through the topic and understand the different types of protectionist measures. It is not necessary to learn the names of all the regional trading blocs but you should have a general awareness of their existence. **Stop and think** What is the current global situation regarding protectionism? To what extent does global free trade exist?	Protectionism can be helpful or harmful to organisations, depending on their position. In the exam you may need to advise on the impact that protectionism has on a particular company or industry.	

Once you have worked through this guidance you are ready to attempt the further question practice included at the end of this chapter.

1 The business environment

Section overview

- Strategy is concerned with matching the organisation to the threats and opportunities in its environment.
- The process of gathering and disseminating the necessary knowledge about a firm's external environment is a specific example of knowledge management.

2.1 Importance of management understanding business environment

The environment contains those factors 'surrounding the organisation'. It includes the general macro-economic environment (the political, economic, social, technological, ecological and legal influences in the countries a business operates in); and factors particular to the firm or industry such as competitors, customers and suppliers.

Figure 1.1: Tiers within the business environment

To be viable (eg, able to sustain itself through time) the organisation must achieve an appropriate 'fit' with this environment. This includes:

- Results that meet the expectations of its owners (shareholders, government, members etc,)
- roducts and services that meet its clients' expectations at least as well as rivals'
- Ability to remain within the legal and ethical codes of the societies it works in
- Attractive as a place to work for its staff
- Satisfying the needs of other powerful or influential stakeholders

Figure 1.2: The rational planning model

(Diagram: The rational planning model)

Rational planning approach: Environmental appraisal is a **one-off assessment** which establishes the forces acting on the business at present and **forecasts** how these may develop during the years of plan.

Strategic management approach: The need for **environmental scanning**. This is a continuous awareness by management of environmental issues enabling them to be routinely considered in decision making.

Interactive question 1: Considering the business environment

For a professional accountancy practice, answer the following questions.

Requirements

1.1 What are the main external factors, in your view?

1.2 How do these main environmental/external factors affect the strategies of the practice?

1.3 In your view, how do managers perceive change in the environment of the organisation?

1.4 How do you think managers incorporate environmental/external issues into decision making?

See **Answer** at the end of this chapter.

Professional skills focus: Assimilating and using information

Strategy development requires detailed analysis of the external environment, using data gathered from a wide range of internal and external sources. The information then needs to be checked for accuracy and relevance before being shared with managers involved in strategy creation.

2.2 Gathering and disseminating environmental information

An effective information system:

- Gathers environmental information.
- Validates and corroborates the information.
- Disseminates the information so that people who need it can find it.

2.2.1 Sources of environmental information

Internal sources include:

- **Employees**: Some will be following developments affecting the firm or their field of work, or have past experiences and networks of contacts that can provide insights.
- **Internal records system**: This will reveal comments of sales teams at meetings, revenue and cost trends at different locations, customer requests or complaints etc.
- **Formal information resources**: Many firms may employ information resources specialists to create current awareness reports eg, accountancy firms have technical departments that monitor changes to regulations and the outcomes of adjudications, test cases and appeals.

External sources include:

- **Trade media**: Magazines and journals specific to the industry or to particular business functions.
- **Published accounts of rivals**, suppliers and clients.
- **Government statistical reports.**
- **Online resources**: Subscriptions to business information vendors, current awareness services (emails from vendors who monitor the media for articles containing keywords specified by management). Social media trends.
- **Market reports**: Published research from investment analysts, market researchers, trade departments of governments etc.

2.2.2 Validating environmental information

Professional scepticism should be applied when considering environmental information. Is it valid and fit for the purpose of analysis? Issues to consider in validating environmental information include:

- Integrity of the source: internet gossip and market rumours lack integrity on their own.
- Forecasting and predictive record in the past.
- Degree of substantiation: is there more than one report or instance of this from independent sources?
- Age of the information: how up to date is it?
- Motivation of provider: does the provider have something to gain from convincing the firm of this information?

Do not assume that information presented in the scenario is factual or relevant. Remember to apply professional scepticism and question the validity of the data.

2.2.3 Disseminating environmental information

Dissemination can be assisted by:

- A well designed intranet with clear files and a search facility. This can be supplemented by regular vlogs and webinars prepared and delivered by management.

- Periodic briefing reports with a digest of the most significant information.
- Periodic seminars to brief management.
- Annual management development sessions at an internal or external business school to introduce and discuss new environmental issues.

3 Environmental dynamics

Section overview

- The ability of the business to plan, and its requirement for information about its external environment, will be influenced by how predictable its environment is.

4.1 Environmental uncertainty

Strategic planning takes place in the context of an uncertain future environment as competitors enter and leave the market, governments and their policies change, technology develops.

Changes in the external environment which have a long-term impact may be dealt with by strategic planning, but dealing with changes that have an immediate short term impact may involve crisis management.

The intensity of environmental issues varies from sector to sector and company to company.

Some businesses exist in relatively **static** environments, where the environment is simple (few competitors, limited products, slow rate of change) but many face environments which are **dynamic** – complex and characterised by rapid change.

In static environments, the business's historic and current environment will be a useful predictor of the future. In dynamic environments this will be of little benefit.

The degree of uncertainty and pace of change will affect the amount of resources devoted to environmental assessment. For example, investment banks employ substantial research departments and each day begins with dissemination of relevant environmental information to traders and managers. Airlines also have research departments which 'red flag' issues on a regular basis and also provide reports and forecasts as inputs into their strategic planning process.

4.2 Scenario planning

Definition

Scenario planning: Concerns the development of pictures of potential futures for the purposes of managerial learning and the development of strategic responses.

4.2.1 When is scenario planning useful?

Scenario planning is useful where a long-term view of strategy is needed and where there are a few key factors influencing the success of the strategy, eg, in the oil industry there may be a need to form a view of the business environment up to 25 years ahead, and issues such as crude oil availability, price and economic conditions are critical. For example, Shell was the only major oil company to have prepared its management for dealing with the shock of the 1970s oil crisis through scenario planning and was able to respond faster than its competitors.

It is important to understand how scenario planning differs in nature from the normal strategic planning exercise. Scenario planning is a wider exercise than simply viewing the entity's operations at a company level and considering a range of external variables likely to impact on the ability of the entity to achieve its objectives. It tries to take a longer term view of the different ways in which an industry may develop. Ultimately, strategic planning results in an organisation developing a strategy, whereas scenario planning is focused on identifying a range of plausible alternatives which give an indication as to the future state of an industry.

Factors such as technology may cause major uncertainty regarding the future shape of an industry (consider for example the impact that email has had on the delivery of letters and that e-readers have had on the book industry.) So in scenario planning a key question might be to consider where the industry will be in 10 years' time. An organisation that wishes to have a sustainable business needs to ask ''what if'' questions and come up with contingency plans.

The nature of scenario planning means that precision is not possible, but it is important to develop a view of the future against which to evaluate and evolve strategies.

Scenario building attempts to create possible future situations using the key factors. The aim is to produce a limited number of scenarios so that strategies can be examined against them in terms of 'what if ...?' and 'what is the effect of ...?'.

A UK-based car manufacturer could assess the impact of 'political changes' or 'opposing moves by competitors' such as the introduction of driver-less cars on its business. Financial models of the firm are often used in conjunction with this approach to assess impact on profit. Although these provide a useful approach, it is important not to become too committed to one scenario; after all, they are only forecasts which might not in the event be valid.

4.2.2 Steps

- Identify key forces which might affect an industry or market, using techniques such as PESTEL analysis (see section 3).
- Understand the historic trend in respect of the key forces.
- Build future scenarios, eg, optimistic, pessimistic and most likely.

The scenarios generated are then 'plots' to be played out making managers consider future possibilities and encouraging them to think about strategy more flexibly. In the chapter Risk management we shall explore the role of scenario building and its use in risk management.

5 *PESTEL analysis*

Section overview

- In your Business, Technology and Finance studies, you will have encountered PESTEL factors in your studies of the environment of business.
- This section provides a recap of the key PESTEL factors and identifies how each may impact on the strategy of the organisation.
- Later sections extend analysis to the global business environment.

6.1 Recap of PESTEL analysis

PESTEL was introduced in Business, Technology and Finance, but we will recap its key themes here. PESTEL is a handy checklist for identifying environmental factors:

- **P**olitical
- **E**conomic
- **S**ocial/cultural
- **T**echnological
- **E**cological/environmental
- **L**egal

PESTEL identifies the macro factors in the external environment which may affect a particular industry. Depending on the industry, some factors will be more significant, eg, legal and ecological issues may have a major influence in the airline industry, whereas political issues will play a major part in the healthcare industry.

The organisation must focus on the key influences currently affecting its industry and those that might become significant in the future ie, the key threats and opportunities that arise for the organisation as a result of the PESTEL analysis.

Professional skills focus: Structuring problems and solutions

In the exam, marks are not awarded for describing the PESTEL model. Instead use PESTEL and other models to structure your answer. This will make it easier for you to analyse the macro-environmental factors that affect the organisation's strategy.

6.2 Political factors

Political factors relate to the distribution of power locally, nationally and internationally.

Political risk is the possibility that political factors will have an impact on the business's environment or prospects. The impact could be positive or negative; the issue is the uncertainty created.

Types of risk include the following:

- **Ownership risk**: A company or its assets might be expropriated (or nationalised) by the state, normally with compensation. Confiscation is, effectively, expropriation without compensation.
- **Operating risk**: **Indigenisation/domestication**. The firm may be required to take local partners. There may be a guaranteed minimum shareholding for local investors.
- **Transfer risk** may affect the company's ability to transfer funds or repatriate profits.
- **Political risk**: The government of the host country may change taxes or seek a stake in the business to increase its power or to satisfy local public opinion.

Managing political risk

Companies, especially transnational corporations, might take measures to reduce political risk. These include:

- Detailed risks assessments prior to investing in the country.
- Partnering with a local business to increase acceptance of the project and to lobby for political support.
- Avoid total reliance on one country, eg, oil companies extract oil from many countries to offset risks of interrupted supplies or spiralling costs.

6.3 Economic factors

The economic structure of a country should be considered in strategic decision-making. Countries typically progress from reliance on primary industries (eg, agriculture, minerals, forestry) through manufacturing to tertiary services (eg, financial and commercial sectors).

A country's economy will affect overall wealth, financial stability and patterns of demand.

In setting strategy an organisation needs to consider where the economy is currently and where it is heading.

- Long-term exchange rates' behaviour affects the relative competitiveness of imported and domestically produced products and exports. A falling domestic exchange rate makes firm's exports more competitive and imported inputs more expensive. This may be determined by the value of key exports such as oil, minerals, crops, manufactured goods etc.
- Interest rates (long-term and short-term) affect cost of finance and also levels of demand in the economy.
- The economic infrastructure, for example access to payments systems, consumer and trade credit, access to venture and other capital, the quality of the stock exchanges.

6.4 Social/cultural factors

Social factors include

- **Make-up of population**: eg, growth rate, proportion of old and young people.
- **Family structure** and size; the importance (or lack of it) of the extended family and relationships with non family members; the extended family provides contacts and work.
- **Attitudes to diversity**: eg, the existence of gender and other stereotypes. In some cultures, gender stereotypes are more sharply drawn.
- Extent of **social mobility**: the degree of social stratification and difference within each society and whether people can move between them, the changes in size, wealth and/or status of different groups within the population and the geographical distribution of the population between regions and urban, suburban and rural areas.

Cultural factors affect strategy in several ways:

- The **market for products**, eg, religious prescriptions on food, financial services
- **Promotional strategies**, eg, language of adverts, considerations of imagery and decency
- **Methods of conducting business** in countries, eg, conventions of negotiation, giving and receiving gifts, ensuring 'face' for contacts (ie, maintaining self-respect and status)
- **Methods of managing staff**, eg, language differences, attitudes to managerial authority
- Expectations of **business conduct**, eg, extent of engagement with corporate responsibility (CR), time horizon of investment, engagement in political matters

6.5 Technology

The strategic significance of the technological environment includes:

- Technological base, and therefore customer and staff familiarity with it, varies across countries. Operations will have to take this into account.
- Technological change challenges existing industry structure and competitive advantages and so strategies to harness or evade it are necessary.
- Technological change can render existing products obsolete but can also provide opportunities to develop new products and ways of doing business. Therefore continuous R&D and learning is necessary to remain competitive. The growing role of technology is explored in greater detail later in the Study Manual.
- Technological change creates uncertainty which may influence the approach to strategy formulation that is adopted.
- Advances in technology may also provide new channels to get products and services to market.
- Technological change in the form of automation and intelligent systems (Artificial Intelligence and Machine Learning) are rapidly changing how organisations structure the activities they undertake, as computers, robots and machines increasingly perform tasks traditionally carried out by people. In the chapter Strategic capability we discuss the topics of automation and intelligent systems in greater detail, when we consider the important area of strategic capability.

6.6 Ecological environment factors

There is an increasing focus on maintaining the world's resources rather than depleting or destroying them, in order to ensure that they support human activity now and in the future.

This desire for 'sustainability' encompasses environmental issues such as:

- **Climate change and pollution**. Global warming is forecast to cause polar ice caps to melt, leading to a chain of events including rises in sea levels and climate change.
- **Energy gap** as fossil fuels diminish while, for example, countries such as Brazil, Russia, India, China and South Africa (the BRICS economies) are growing rapidly and demand more energy.
- **Waste recycling** issues as developed countries recognise the forecast use of landfill and also realise that much landfill is hazardous waste (eg, batteries, electronic circuitry, oil and solvents in car engines).
- **Bio-diversity** issues as growing of cash crops and destruction of forests for grazing or building land also destroys species of plant, insects and animals.
- Introduction of **genetically modified organisms** into the food chain leading to loss of species and potentially hazardous future effects.

Main government policies are:

- Reduce carbon emissions through targets set in cross governmental accords such as the 1992 Kyoto and 2015 Paris agreements.
- Penalisation of carbon creating industries through taxes levied on emissions or on fossil fuels used.
- Investment in non-carbon creating technologies such as nuclear energy, wind and wave power and electric or hybrid cars.
- Making foreign aid dependent on acceptance of environmental policies by recipient countries.
- Regulations covering hazardous waste.

Implications for business strategy

- Need to accept 'polluter pays' costs – taxes on emissions and requirements that firms buy certificates from refuse firms confirming recovery or destruction of materials the firm introduces into the supply chain.
- Increased emphasis on businesses acceptance of corporate responsibility (CR) and principles of sustainable development.
- Potential for economic gain from cleaning-up operations and selling surplus 'permits to pollute' to firms that have not cleaned up.
- Potential competitive advantage from development of products that ecologically conscious buyers will favour.
- Need to monitor ecology-related geo-political and legislative developments closely.

6.6.1 Natural capital

Linked to the concept of ecology and sustainability is that of natural capital, climate change and green finance.

Definition

Natural capital: The 'natural assets (eg, air, water, land, habitats) that provide everyday resources including timber, agricultural land, fisheries and clean water as well as services such as air and water filtration, flood protection and pollination for crops (otherwise known as 'ecosystem services') (Dunscombe and Glover, 2016:p.2, *Natural capital in practice*, ICAEW).

The focus on natural capital has increased dramatically in recent years as organisations begin to better understand how their activities affect the natural world. The Natural Capital Forum (2018) compares the concept of natural capital to that of an organisation spending more than it earns, in as much that it will eventually run up a debt. When organisations take more out of the natural environment than they give back, they have run up a debt which needs to be paid back. This can be achieved, for example, through repairing the damage caused by polluting activities, or replanting forests where trees have been felled to provide timber for production. Organisations that 'keep drawing down stocks of natural capital without allowing or encouraging nature to recover, run the risk of local, regional or even global ecosystem collapse. Poorly managed natural capital therefore becomes not only an ecological liability, but a social and economic liability too'. (Natural Capital Forum, 2018).

The increasing focus on natural capital is starting to change the way in which organisations report on their activities, with many now attempting to place financial values on the natural assets they use, to enable them to make more informed business decisions.

We will look at the increasing focus on sustainable business practices and sustainability reporting in more detail in the chapter Ethics, sustainability and corporate responsibility.

Definition

Green finance: Green finance can refer to financial investments into environmental goods and services, for example the protection of biodiversity. It can also refer to schemes to encourage sustainability, such as policies to encourage investment in renewable energies. Green finance can also specifically relate to the financial systems that deal with green investments, which are known as green bonds and green funds.

The UK government launched its Green Finance Strategy in July 2019 with two main objectives. Firstly, the strategy aims to align investment and cashflows generated by the private sector with sustainable growth. The second objective is to ensure that any green initiatives lead to a strengthening of UK financial sector competitiveness. There are three pillars to the government strategy;

(a) Greening finance - ensuring that financial decision-making takes account of the risks and opportunities generated by climate and environmental issues. For example, decisions need to take account of the potential risk of asset damage, arising from an increase in extreme weather events.

(b) Financing green - encouraging public and private investment in sustainable energy and other projects to help achieve carbon targets. For example, between 2015 and 2021 the UK government will have invested nearly £1.5 billion in schemes to provide charge point infrastructure for electric vehicles.

(c) Capturing the opportunity - ensuring UK financial services capture the commercial opportunities generated by the increase in climate data and analytics as well as from new green financial products and services.

(Great Britain. Department for Business, Energy and Industrial strategy., (2019). *Green Finance Strategy. Transforming Finance for a Greener Future*. London: HMSO.)

In response to the government's strategy ICAEW has signed up to the Green Finance Education Charter to ensure that today's accountants are fully versed in green finance and are able to consider and report on the impact that strategic decisions may have on the environment.

6.7 Legal factors

Legal factors relate to the role of law in society and its role in business relationships. This can be assessed in terms of:

- **Systemic factors**: How effective is the legal system at enforcing contracts? To what extent are legal decisions likely to be interfered with by politicians ie, are the courts independent of government? How easy is it to get hold of legal advice? How speedy are the courts? To what extent is regulation delegated? Are rights of private property genuinely enforceable?
- **Cultural factors**: To what extent are business relationships conducted formally or informally? The USA is regarded as a litigious society; in Japan (partly because of the small size of the legal profession), business is widely believed to be based more on long-term relationships.
- **Context and regulatory factors**: Cover civil and criminal law, laws relating to consumer protection and advertising, employment, health and safety and so forth. Furthermore, to what extent is competition promoted, regulated and enforced? Intellectual property rights are examples of specific issues which need to be considered.

Context example: Context example: estate agent industry

Estate agents are residential property agencies which act on behalf of individual vendors to assist in the sale of their home. Revenues are derived from financial services, lettings, valuations and surveys. However, the main source of revenue is commissions on the sale of residential property.

Agencies are regulated in the UK by the Estate Agents Act 1979, which aims to ensure that agents act in the best interests of sellers, and that both buyers and sellers are treated honestly and fairly. Agencies must also comply with money laundering legislation. Agency employees are not currently required by UK law to be either licensed or formally qualified. However, many employees belong to a professional body and must comply with that body's code of professional ethics.

In recent times traditional estate agents operating physical branches have struggled. The traditional estate agency business model has suffered as a direct consequence of the continuing rise of technology start-up companies which are now challenging existing ways to sell property. The rise of so-called 'proptech' firms has seen increasing numbers of house sellers turn to online estate agencies like Purplebricks.

Unlike traditional estate agents, which operate from physical branches often located on busy UK high streets employing teams of estate agents, companies like Purplebricks operate a hybrid strategy. This strategy does not require the use of high street branches as the company operates from an online platform where sellers are assisted through the selling process by a dedicated property expert contracted on a freelance basis by Purplebricks. Websites charge private sellers commission fees which are a fraction of those being charged by traditional estate agents. One online article (Thomas, 2019) reported that Purplebricks controlled 69% of the online estate agency market. In recent times, a number of established estate agencies have invested in similar online 'proptech' companies in recognition of the changes this is creating in the industry. It is estimated that online agencies represented sellers in 15% of UK property sales in 2018.

In early 2017, the UK government announced plans to help first-time buyers to get onto the property ladder by allowing councils to build houses on hundreds of brownfield sites, being land which was previously deemed unusable. A second newspaper article (McCann, 2017) highlighted that the government's financial support for the scheme would see housing developers sell the properties at a discount of 20%, to help first-time buyers. In November 2017, changes were made to the stamp duty thresholds in the UK with the aim of making it cheaper for first-time buyers to purchase property. (In the UK when a buyer purchases a home they pay a tax known as stamp duty, and the amount of tax paid depends on the value of the property.) The changes meant that first-time buyers purchasing a property with a value up to £300,000 would not have to pay stamp duty, and thereby able to save thousands of pounds in tax. However, some observers have suggested that the stamp duty changes have in fact slowed the first-time buyer property market, as buyers were instead choosing to wait longer, save more, and then purchase a larger property from which they could eventually start a family, instead of purchasing a smaller home first (Morley, 2018).

A common feature of the UK housing market for a number of years has been rising property prices. According to the Royal Institution of Chartered Surveyors, the growth in house prices in the UK had been caused by a shortage in the number of properties coming onto the market coupled with increases in the number of buyers (Osborne, 2016). The population in the UK is expected to reach 73 million people by 2037, with an increase in the requirement for single occupant households as the demographics in the UK change. This is predicted to increase the demand for houses in the long term.

Sources:

Osborne, H. (26 December 2016) UK housing market: what to expect in 2017. *The Guardian*. [Online] Available from: www.theguardian.com [Accessed 25 April 2017].

McCann, K. (3 January 2017) Theresa May promises thousands of new homes for young first-time buyers. *The Telegraph*. [Online] Available from: www.telegraph.co.uk [Accessed 25 April 2017].

Morely, K. (27 February 2018) Stamp duty changes slowing first-time buyer market as they shun flats for family homes. *The Telegraph*. [Online]. Available from: www.telegraph.co.uk [Accessed 19 April 2018].

Thomas, O. (7 February 2019) Purplebricks dominates online estate agents with 69% market share. *Mortgage Solutions*. [Online]. Available from: www.mortgagesolutions.co.uk/news/2019/02/07/purplebricks-dominates-online-estate-agents-with-69-market-share/ [Accessed 26 April 2019].

Interactive question 2: Estate agent industry

The following interactive question provides an opportunity for you to apply the PESTEL framework to the UK estate agent industry.

Requirement

Discuss the environmental factors that affect the estate agent industry, using the following headings

(1) Political

(2) Economic

(3) Social

(4) Technological

(5) Ecological

(6) Legal

See **Answer** at the end of this chapter.

7 The international business context

Section overview

- Few if any businesses are unaffected by global influences from competition, new markets or, at the very least, cheaper sources of supply.
- The view that certain nations have built-in advantages from low costs or harder-working staff has given way to a more sophisticated view that home factors may configure to give advantages to a handful of specific industries.
- This is illustrated using – Porter's Diamond model.

8.1 The importance of the global business environment

Rapid industrialisation from the 18th century was a consequence of early involvement of merchants and businesses in trade. In the 21st century improved transportation and communications and cross-border business ownership have created, for most industries, a global business environment.

Global competition affects firms in several ways.

- It provides the opportunities of new markets to exploit.
- It presents the threat of new sources of competition in the home economy from foreign firms.
- It offers an opportunity of relocating parts of business activity (or **supply chain**) to countries able to perform them better or more cheaply.
- It may drive cross border acquisitions and alliances.

This leads management to make significant strategic investment decisions that rely on assessments of the stability and trends of the global business environment:

- Development of products for international markets.
- Advancing credit to clients in international markets or investing in businesses and assets in host countries.
- Reliance of international sources for supplies of crucial inputs.

8.2 The global corporation

Definition

Globalisation: The production and distribution of products and services of a homogenous type and quality on a worldwide basis.

Levitt (*The Globalisation of Markets,* 1983) described the development of a 'global village' in which consumers around the world would have the same needs and attitudes and use the same products. A global corporation would be one that operated as if the entire world was one entity, to be sold the same things everywhere.

Levitt's focus was on the marketing aspects of globalisation. The global business corporation will also be characterised by:

- **Extended supply chains**: Instead of making the product at home and exporting it, or setting up a factory in the host country to make it, the global corporation may factor out production so that different parts of the product (or service) originate in different countries. Womack et al (*The Machine That Changed The World*) suggest that the globalisation of the automobile industry led the way for this model.
- **Global human resource management**: This involves pan-national recruitment and development of human resources.

Interactive question 3: A global corporation

Some would say that such purely global organisations are rare. Industry structures change and foreign markets are culturally diverse. Even within the USA, there is an enormous variety of cultural differences.

Requirement

Can you think of a global corporation that fulfils the requirements of the definition given above?

See Answer at the end of this chapter.

See **Answer** at the end of this chapter.

8.3 Ohmae's five Cs: factors encouraging development of global business

Ohmae (*The Borderless World*) has identified a number of reasons which might encourage a firm to act globally arranged into a 'five C's' framework.

The customer	Are consumer tastes across the world converging upon similar product characteristics?
The company itself	Selling in a number of markets enables fixed costs to be spread over a larger sales volume.
Competition	The presence of global competitors, who are enjoying the benefits of global commitment, could encourage a previously local or regional operator to expand its activities.
Currency volatility	Setting up assembly overseas is a way of reducing the exchange rate risks inherent in exporting and may also help to get around government imposed trade barriers.
Country	Locating business activities overseas may provide cheaper access to labour, materials and finance, along with the goodwill of host governments.

The continuing political acceptance of free-trade by international economies is essential to the success of these strategic investments.

8.4 Porter's Diamond: The Competitive Advantage of Nations

Management developing strategy in a global environment needs to understand the competitive advantages they have over firms from other countries.

Porter (*The Competitive Advantage of Nations*) seeks to 'isolate the national attributes that foster competitive advantage in an industry'.

Porter identifies determinants of national competitive advantage which are outlined in the following diagram. Porter refers to this as the Diamond.

Figure 1.3: Porter's Diamond

Role of factor conditions	Basic factors	Advanced factors

Role of factor conditions	Basic factors	Advanced factors
Human resources skills, (price, motivation, industrial relations) Physical resources (land, minerals, climate, location relative to other nations) Knowledge (scientific and technical know-how, educational institutions) Capital (ie, amounts available for investment, how it is deployed?) Infrastructure (transport, communications, housing)	Basic factors include: natural resources, climate, semi-skilled and unskilled labour. Basic factors are inherited, or at best their creation involves little investment.	Advanced factors include modern digital communications, highly educated personnel, research laboratories and so forth. They are necessary to achieve high order competitive advantages such as differentiated products and proprietary production technology.

Role of demand conditions	Comment
The home market determines how firms perceive, interpret and respond to buyer needs. This information puts pressure on firms to innovate and provides a launch pad for global ambitions.	• There are few cultural impediments to communication in the home market. • The segmentation of the home market shapes a firm's priorities: companies will generally be successful globally in segments which are similar to the home market. • Sophisticated and demanding buyers set standards. • Anticipatory buyer needs: if consumer needs are expressed in the home market earlier than in the world market, the firm benefits from experience. • The rate of growth: slow growing home markets do not encourage the adoption of state of the art technology. • Early saturation of the home market will encourage a firm to export.

Role of related and supporting industries	Comment
Competitive success in one industry is often linked to success in related industries. Domestic suppliers are preferable to foreign suppliers, as 'proximity of managerial and technical personnel, along with cultural similarity, tends to facilitate free and open information flow' at an early stage.	This facilitates the generation of clusters. These are concentrations of many companies in the same industry in one area, together with industries to support them. For example, London in the UK is a global financial services centre, with a concentration of banks, legal services, accounting services and a depth of specialist expertise. Silicon Valley is a further example.

Role of strategy, structure and rivalry	Comment
Structure	National cultural factors create certain tendencies to orientate business people to certain industries. German firms have a strong presence in industries with a high technical content.
Strategy	Industries in different countries have different time horizons, funding needs and so forth. • National capital markets set different goals for performance. In some countries, banks are the main source of capital, not equity shareholders.

Role of strategy, structure and rivalry	Comment
	• When an industry faces difficult times, it can either innovate within the industry, to sustain competitive position or shift resources from one industry to another (eg, diversification).
Domestic rivalry	• With little domestic rivalry, firms are happy to rely on the home market. • Tough domestic rivals teach a firm about competitive success. • Each rival can try a different strategic approach.

Two other variables, **chance events** and the **role of government**, also play their part in determining the competitive environment.

8.4.1 Interactions between the determinants

The factors in the 'Diamond' are interrelated. Competitive advantage in an industry rarely rests on a single determinant.

- Related industries affect demand conditions for an industry. For example 'piggy-back' exporting is when an exporting company also exports some of the products of related industries.
- Domestic rivalry can encourage the creation of more specialised supplier industries.

8.4.2 Clusters

Related business and industries are geographically clustered. A cluster is a linking of industries through relationships which are either vertical (buyer-supplier) or horizontal (common customers, technology, skills). Clusters are supposedly a key factor in the competitive advantage of nations.

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Figure 1.4: Industry links in a cluster

Within a country, the industry may be clustered in a particular area.

- The Indian software industry is based in Bangalore.
- The UK investment banking industry is largely based in London.

Interactive question 4: Why do banks cluster?

It is easy to see why mining companies should congregate in a cluster around coal seams, or shipping services would congregate around ports, but why should banks and software companies be clustered in the same way, given plentiful IT and broad bandwidth communications?

See **Answer** at the end of this chapter.

8.4.3 Using Porter's Diamond to develop business strategies

Porter claims that firms gain competitive advantage from either of two sources.

- Lower costs of supply to customers which result in higher profitability (cost leadership).
- Differentiated service or reputation resulting in higher prices and sales revenues (differentiation).

Porter advises management to consider the diamond factors in their home country and to compare them with the diamond factors available to rivals from other countries.

He offers the following prescription.

- If the home diamond factors give a comparative cost advantage over those of foreign rivals then management should adopt strategies based on **overall cost leadership**. This may explain the strategies of South Korean car manufacturers like Hyundai/Kia, Daewoo and SsangYong (the latter two being respectively offshoots of General Motors and Daimler Chrysler).

- If the home diamond factors give a differentiation advantage over foreign rivals management should adopt strategies based on **differentiation**. This may explain why car manufacturers Mercedes, BMW and Audi tend to develop and initially produce their limousines in Germany but build vans and utility cars in Spain, South Africa and Brazil.
- If the diamond does not confer advantage over rivals then management must **focus** on sub-sections of the industry which large players may have overlooked or not be able to exploit commercially. This may explain the large number of private banks in Switzerland or the boutique sports car makers in Italy (Ferrari, Lamborghini, Maserati etc).

Context example: Context example: Chinese car industry

At the end of the 20th century, China's car production did not match any single large auto company in the developed world. In 2019 the International Organization of Motor Vehicle Manufacturers reported China was the world's largest car producer in 2018. But it is not just volumes. China's car makers now produce not just low-cost runabouts, but also luxury and sports models, 'concept cars' and even a few hybrid and electric vehicles. Local car makers in the fastest-growing car market would appear to have come of age.

Until recently many Chinese car makers built thinly-disguised copies of vehicles made by Volkswagen, GM and Toyota. In the past few years things have changed. In preparation for a push overseas local firms such as Chery, Great Wall and Geely have proved they can develop their own vehicles too. Buying designs from international specialists and installing robotic production lines have led to an increase in the types of cars produced.

For a number of years foreign car makers had been worried by the Chinese firms' ultra low prices, however this has been changing in recent times. The rise of China's affluent middle class has led increasing numbers of Chinese consumers to switch to more expensive Western brands renowned for safety and flair. Chinese domestic car brands have also been damaged by poor safety crash results. Chinese cars exported today mostly go to Africa, south-east Asia and the Middle East, where expectations are lower and price matters more.

The development of China's car manufacturing business has been helped by a number of factors. A lot of early technology was borrowed. The government also offered support to fledgling firms via direct investments, guaranteed loans and a programme aimed at supporting Chinese production of electric cars. Universities provided technical help, especially in the development of expensive engines. Future legislation is likely to force foreign firms to do more research and development in conjunction with Chinese partners to ensure continued access to cutting-edge engineering skills.

Source:

International Organization of Motor Vehicle Manufacturers. (2019) *2018 Production Statistics*. [Online]. Available from: http://www.oica.net/category/production-statistics/2018-statistics/[Accessed 26 April 2019].

Interactive question 5: Chinese car industry

Identify, using Porter's Diamond, the sources and nature of any competitive advantage enjoyed by Chinese car manufacturers.

See **Answer** at the end of this chapter.

9 Limits to globalisation of business

Section overview

- Despite the forecasts there are many impediments to the development of global businesses such as protectionism. These are reviewed here.
- Pursuing a global strategy is a source of risk to a business, either because the forecast opportunity doesn't come about or because host governments change their policies towards 'foreign' investment and render it no-longer valuable.

10.1 Political risks in international business

The development of plans for international business will depend on the following factors:

(a) The stability of the government. Rapid changes or political unrest make it difficult to estimate reactions to an importer or a foreign business.

(b) International relations. The government's attitude to the firm's home government or country may affect trading relations.

(c) The ideology of the government and its role in the economy will affect the way in which the company may be allowed to trade, and this might be embodied in legislation.

(d) Informal relations between government officials and businesses are important in some countries. Cultivation of the right political contacts may be essential for decisions to be made in your favour.

Political risk is still relevant with regard to overseas investment, especially in large infrastructure projects overseas. History contains dismal tales of investment projects that went wrong, and were expropriated (nationalised) by the local government.

- Suspicion of foreign ownership is still rife, especially when prices are raised.
- Opposition politicians can appeal to nationalism by claiming the government sold out to foreigners.
- Governments might want to re-negotiate a deal to get a better bargain, at a later date, thereby affecting return on investment.

In addition to expropriation, there are other dangers:

- Restrictions on profit repatriation (for example, for currency reasons).
- 'Cronyism' and corruption leading to unfair favouring of some companies over others.
- Arbitrary changes in taxation.
- Pressure group activity.

Context example: Context example: Brexit

A good example of political risk and uncertainty in international business concerns the UK's decision to leave the European Union, following a referendum in June 2016. In March 2017 Sir Tim Barrow, the UK's ambassador to the EU, submitted a letter to EU Council President Donald Tusk formally triggering the two year process of the UK's withdrawal from the EU. Since this time many business leaders have expressed concern over the uncertainty surrounding the eventual trading relationship that Britain will have with its European neighbours when the country leaves the EU. In response, many large multinational businesses in a range of sectors have turned to various forms of scenario planning to better understand the potential impact that the failure of the UK and the EU to reach a tariff-free trade deal would have on their respective industries.

The UK officially left the European Union on 31st January 2020 with a transition period in place until the end of 2020, for the British government to negotiate and establish new rules on trade, travel and business. However, until new rules and terms of trade have had time to become established, uncertainty for business remains.

10.2 Protectionism in international trade

Protectionism is the discouraging of imports by, for example, raising tariff barriers and imposing quotas in order to favour local producers. It is rife in agriculture.

Protectionist measures include:

Tariffs or customs duties: A tax on imports where the importer is required to pay either a percentage of the value of the imported good (an *ad valorem* duty), or per unit of the good imported (a specific duty).

Nontariff barriers: Restrictions on the quantity of product allowed to be imported into a country. The restrictions can be imposed by import licences (in which case the government gets additional revenue) or simply by granting the right to import only to certain producers.

Minimum local content rules: A specified minimum local content of products should be made in the country or region in which they are sold to qualify as being 'home made' and so avoid other restrictions on imports. This leads manufacturers to set up factories in the country.

Minimum prices and anti-dumping action: To stop the sale of a product in an overseas market at a price lower than charged in the domestic market, anti-dumping measures including establishing quotas, minimum prices or extra excise duties are used.

Embargoes: A total ban or zero quota.

Subsidies for domestic producers: Financial help and assistance from government departments that give the domestic producer a cost advantage over foreign producers in export as well as domestic markets.

Exchange controls and exchange rate policy: Regulations designed to make it difficult for importers to obtain the currency they need to buy foreign goods.

Unofficial non-tariff barriers: Administrative controls such as slow inspection procedures or changing product standards which are hard for foreign suppliers to anticipate and respond to.

10.3 Trade blocs and triads

Trading blocs

Currently, a number of regional trading arrangements (or 'blocs') exist, as well as global trading arrangements. These regional trading groups take three forms.

(a) Free trade areas – members in these arrangements agree to lower barriers to trade amongst themselves, eg, NAFTA (USA, Canada, Mexico). NAFTA will be replaced with the United-States-Mexico-Canada-Agreement (USMCA) once ratified by the three member states.

(b) Customs unions – these agree a common policy on barriers to external countries. Tariffs, taxes and duties are harmonised amongst members.

(c) Common markets – in effect, the members become one trading area. There is free movement of all factors of production. The European Union (EU) features a common political decision making process and a single currency and has economic union as an aim.

In addition to NAFTA and the EU, other major regional trade organisations include:

- Mercosur – Brazil, Argentina, Paraguay and Uruguay (Venezuela's membership was suspended in 2017)
- The Economic Community of West African States (ECOWAS)
- The Association of Southeast Asian Nations (ASEAN) – Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, Cambodia, Laos, Myanmar , and Vietnam.

Triad theory describes the international business environment as a limited number of 'superblocs'.

The Triad

Ohmae developed the concept of a global economic triad in 1985, consisting of three main economic blocs: the USA, the EU and Japan, which controlled 75% of world trade at the time.

Triad theory rejects the idea that homogenous products can be developed and sold throughout the world. Multinationals have to develop their products for the circumstances of each triad.

The Triad theory which applied in the latter part of the 20th century may be out of date now. The emerging markets, particularly those of China and India, but also Eastern Europe may give rise to additional trading blocs or a shifting economic triad for the 21st century of China, India and the US.

Summary

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Self-test

Answer the following questions.

(a) PDB Motors plc is a major UK car manufacturer with plants in the UK and Europe. It is seeking to exploit both the buoyant North American and Brazilian markets for car sales.

Suggest two reasons why it would be a logical strategy for PDB Motors plc to build an assembly plant in Mexico.

(b) Social and technological factors always need to be assessed when analysing the environment within which a business operates.

Give two examples of each of these factors which would be relevant to Busline plc, a UK operator of coach tours to Scarborough and Whitby (seaside towns in the North of England).

Suggest how each of your factors may impact future demand.

(c) Read the scenario of the **September 2018 Business Strategy and Technology** question in the Question Bank titled *Vision Bank*. Draft an answer to the question which requires an analysis of three key external factors using relevant models.

(d) Read the scenario of the **March 2017 Business Strategy and Technology** question in the Question Bank titled *Ignite plc*. Draft an answer to the question which requires the analysis of the external factors that have influenced the changing demand for Ignite's cigarette lighters.

Now, go back to the Learning outcomes in the Introduction. If you are satisfied that you have achieved the objective, please tick it off.

Answers to Self-test

- Two reasons from the following:
  - This would allow PDB to take advantage of low labour costs in Mexico.
  - The location would be close to potential major markets, cutting transport costs and reducing lead time.
  - The North American Free Trade Agreement (NAFTA) will avoid sales to the USA and Canada being subject to import restrictions.
  - It delivers sales growth prospects to a company facing a saturated European market.
- **Social factors**

Two examples form the following:

- Increasing car ownership (lower demand)
- Higher proportion of older people in society (higher demand)
- Cheap overseas packages available (lower demand)
- **Technological factors**
- Two examples from the following:
- Development of faster trains (lower demand).
- More comfortable coaches being developed (higher demand).

- Greater internet accessibility, creating more awareness of other travel options (lower demand). However, the ability to book coach tour tickets online coupled to a dynamic pricing approach may actually increase demand (higher demand). Furthermore, customers may demand improved functionality when using coaches, for example, free Wi-Fi.
- Refer to the answer to Vision Bank in the Question Bank.
- Refer to the answer to Ignite plc in the Question Bank.

Further question practice

1 Knowledge diagnostic

Before you move on to question practice, complete the following knowledge diagnostic and check you are able to confirm you possess the following essential learning from this chapter. If not, you are advised to revisit the relevant learning from the topic indicated.

Confirm your learning	
1.	Do you understand the various sources of information and their limitations? (Topic 1)
2.	Can you explain the benefits of scenario planning and list the stages involved? (Topic 2)
3.	Can you conduct a PESTEL analysis of the macro-environment? (Topic 3)
4.	Can you explain Ohmae's five Cs for encouraging global business operations? (Topic 4)
5.	What are the limits and risks inherent in globalisation? (Topic 5)

2 Question practice

Aim to complete all self-test questions at the end of this chapter. The following self-test questions are particularly helpful to further topic understanding and guide skills application before you proceed to the next chapter.

Question	Learning benefit from attempting this question
1	This question is designed to encourage the generation of ideas. There are no relevant models or theories you can use so rely on commercial acumen and general business awareness instead.
2	Question 2 requires you to assess two macro-environmental factors; social and technological. It is important to explain how these factors impact future demand rather than simply describing them.

Once you have completed these self-test questions, it is beneficial to attempt the following questions from the Question Bank for this module. These questions have been selected to introduce exam style scenarios that will help you improve your knowledge application and professional skills development before you start the next chapter.

Question	Learning benefit from attempting this question
Vision Bank (Sept 2018)	Part 1 of the question requires you to analyse three external factors influencing banking. You are asked to refer to relevant models but are not told which ones to use. Ensure you understand which external environment models are useful and relevant in which circumstances.
Ignite plc (March 2017)	Part 1 requires an environmental analysis supported by data in two exhibits. The first exhibit contains a graph with some company history. The second exhibit provides key dates. You are also able to attempt part 2 examining the company's product portfolio using the BCG matrix. Remember to apply your answers to the detailed scenario information provided.

Refer back to the learning in this chapter for any questions which you did not answer correctly or where the suggested solution has not provided sufficient explanation to answer all your queries. Once you have attempted these questions, you can continue your studies by moving on to the next chapter.

Self-test questions

Answer the following questions.

- PDB Motors plc is a major UK car manufacturer with plants in the UK and Europe. It is seeking to exploit both the buoyant North American and Brazilian markets for car sales.

  Requirement

  Suggest two reasons why it would be a logical strategy for PDB Motors plc to build an assembly plant in Mexico.

- Social and technological factors always need to be assessed when analysing the environment within which a business operates.

  Requirement

  Give two examples of each of these factors which would be relevant to Busline plc, a UK operator of coach tours to Scarborough and Whitby (seaside towns in the North of England).

  Suggest how each of your factors may impact future demand.

- Read the scenario of the **September 2018 Business Strategy and Technology** question in the Question Bank titled *Vision Bank*.

  Requirement

  Draft an answer to the question which requires an analysis of three key external factors using relevant models.

- Read the scenario of the **March 2017 Business Strategy and Technology** question in the Question Bank titled *Ignite plc*.

  Requirement

  Draft an answer to the question which requires the analysis of the external factors that have influenced the changing demand for Ignite's cigarette lighters.

Now go back to the Introduction and ensure that you have achieved the Learning outcomes listed for this chapter.

Answers to Interactive questions

Answer to Interactive question 1

1.1 External factors would include:

- Rival accounting firms seeking to take clients themselves.
- Other professional practices which may direct work toward us
- Regulations such as tax laws, accounting standards and audit standards.
- The labour market for post-qualified and qualified accountants.
- The general state of the economy and its effect on business.

1.2 These factors create opportunities and threats. New regulations create a need for professional advisers to provide guidance to clients. Competitors or a thriving labour market with higher pay create threats (incidentally notice how you changed your perspective on the last point because you would like to have the higher pay but you are calling it a threat for your firm). This illustrates how flawed the distinction between 'internal' and 'external' is when we discuss environmental analysis.

1.3 This will depend on the managers' psychological make-up. Some will see it as a tiresome bind that makes them have to keep changing things and also which makes it hard to plan or feel certain. Others will see it as invigorating.

A very interesting test of management is the extent to which they see themselves as powerless in the faces of environmental changes or whether they believe they can shape and respond to them.

1.4 Again, this varies. Some will avoid making decisions which could be affected by environmental uncertainty, and will wait till it settles down (hence incrementalism). Some will simply ignore environmental issues that cannot be proven. Perhaps a more balanced approach is to adopt strategies that would still deliver benefit under a number of environmental developments or perhaps have several courses of action running at the same time, with each one designed to take advantage of different environments. In another context, energy companies invest in several different technologies because they do not know how oil prices and environmental regulations will develop.

Answer to Interactive question 2

The factors affecting the estate agent industry are very closely linked to prosperity and activity in the residential housing market. The PESTEL analysis therefore needs to consider the wider housing market as well as factors directly affecting the estate agent industry.

(1) **Political**

Political influences relate to the extent to which it is government policy to support and promote the housing market. The UK government's plans to help first-time buyers get onto the property ladder by allowing the development of brownfield sites is aimed at increasing the national housing stock. The planned subsidisation in the form of the 20% discount for first-time buyers removes a barrier to buying a house. The government's scheme is likely to be positive for the UK estate agency industry if the new homes are sold through those estate agents in close proximity to the brownfield sites.

The proposal to remove stamp duty for first-time buyers purchasing houses for less than £300,000 was also designed stimulate demand. However, this initiative may not be as positive for estate agents as might have first been expected, because some buyers are choosing to delay purchasing a home in order to allow them to purchase a larger property in the future.

(2) **Economic**

Political considerations are closely linked to economic factors. The dependence of the housing market on the prosperity of individuals is heavily influenced by the success of the government's economic policy. Despite the growth in house prices, traditional estate agents have struggled to capitalise. The buoyancy of the economy generally and the housing market in particular appears to have helped new start-up firms to enter the industry to compete with established players.

(3) **Social**

The increasing population and the change in demographics have expanded the long run potential growth of the housing market. In particular the increased proportion of single occupancy dwelling increases the volume, but changes the mix, of desired housing. Whilst this may appear to be positive for estate agents in general, social changes in how people buy and sell property are undermining the ability of traditional estate agents to benefit from the demographic changes. The rise of online estate agents, which provide services at lower fees than those charged by traditional agents, suggests that sellers do not regard the service offering of existing players to be worth paying for. The rise of companies such as Purplebricks is considered in the following section on technological factors.

(4) **Technological**

Increased usage of the internet, and other electronic means of communication, is a threat to estate agents as a substitute sales channel for direct transactions between buyer and seller. The significance of this threat is evident as Purplebricks alone controls 69% of the UK online estate agency market. The ability of such a relatively new player to become established in the online estate agency market is likely to increase the difficulty in the long-term for traditional players to compete. Furthermore, as a number of established estate agents have invested in 'proptech' companies this indicates that they perceive an increasingly greater role for online estate agents in the future. Despite these changes in 2018 online agents were estimated to have been involved in just 15% of all property sales made in the UK, all of which reduces the short-term significance of the threat posed to traditional estate agents.

(5) **Ecological/environmental**

The UK governments proposal to allow councils and developers use brownfield sites indicates a willingness to make better use of land previously deemed unacceptable for development. This will reduce the price of new houses for eligible first-time buyers, and may result in increased business for estate agents in the event the house builders choose to sell via an agent.

(6) **Legal**

Legal issues can be both a benefit and a cost to the industry. Legislation may directly affect the practices of estate agents, but could also have an impact upon the housing market (as we have already noted in relation to stamp duty). In the UK, estate agents are required to comply with two key pieces of legislation: the Estate Agents Act 1979, and Money Laundering regulations. The need to comply with the provisions of such legislation will attract its own costs, in terms of providing staff with relevant training and paying penalties for any breaches.

Answer to Interactive question 3

Levitt cited examples such as Coca-Cola in his article. More recently, examples such as Starbucks, Mercedes Benz, Facebook, Google, Microsoft and Disney have been called global businesses.

In practice, these corporations offer subtly different products in different markets and their appeal is not global. For example, Coca-Cola has suffered badly from an anti-American sentiment.

Answer to Interactive question 4

The reasons cited for geographical clustering of financial and IT businesses are:

- Proximity to educational and research centres. For example, in USA the IT industry clusters around its universities.
- Networking and mutual exchanging of staff.

Answer to Interactive question 5

The scenario suggests the following sources of the cost leadership advantages enjoyed by the Chinese car industry:

Demand conditions: China is a very large market and fast growing. This enables firms to gain significant economies of scale and also to justify investment in the new models and production equipment. Although demand is still high for domestic brands this appears to be changing as the number of affluent Chinese middle-class buyers continues to grow. Buyers from this group are now preferring to purchase foreign models. Historically, demand in China was driven for low price cars and which had forced car makers to concentrate on reducing costs.

Related industries: The only cited example is the assistance from universities in R&D. This provides significant cost advantages compared with in-house development. The low price of the Chinese vehicles suggests that steel and other components are being sourced cheaply too.

Factor conditions: China clearly has a good technical education system. It is also known for having abundant cheap labour and land available for building car plants. It has good sea links and freight handling for the purposes of exporting.

Firm strategy, structure and rivalry: The Chinese government is keen for the market to achieve future growth among Chinese brands and has put in place measures to support local car makers. This will give each significant economies of scale and an incentive to invest in product and process improvement. That foreign-made cars are allowed into China gives a stimulus to product development and the search for competitive advantage.

Answers to Self-test questions

1 Two reasons from the following:
   - This would allow PDB to take advantage of low labour costs in Mexico.
   - The location would be close to potential major markets, cutting transport costs and reducing lead time.
   - The North American Free Trade Agreement (NAFTA) will avoid sales to the USA and Canada being subject to import restrictions.
   - It delivers sales growth prospects to a company facing a saturated European market.

2 Social factors

3 Two examples form the following:
   - Increasing car ownership (lower demand)
   - Higher proportion of older people in society (higher demand)
   - Cheap overseas packages available (lower demand)

Technological factors

4 Two examples from the following:
   - Development of faster trains (lower demand).
   - More comfortable coaches being developed (higher demand).
   - Greater internet accessibility, creating more awareness of other travel options (lower demand). However, the ability to book coach tour tickets online coupled to a dynamic pricing approach may actually increase demand (higher demand). Furthermore, customers may demand improved functionality when using coaches, for example, free Wi-Fi.

5 Refer to the answer to Vision Bank in the Question Bank.

6 Refer to the answer to Ignite plc in the Question Bank

Appendix

Tax Tables FA2020

Syllabus area: Administration

SUBMISSION DATES

Submission dates for 2020/21 personal self-assessment tax returns

Return filed online	Later of: 31 January 2022 3 months from the date of issue of return
Paper returns	Later of: 31 October 2021 3 months from the date of issue of return

Submission dates for corporation tax returns

Must be filed by 12 months from the end of the period of account.

Submission dates for PAYE information: Real Time Information

Information	**Filing date**
Full Payment Submission (FPS)	On or before the day the employee is paid
P60 (to employees)	31 May following the tax year end
P11D	6 July following the tax year end

PAYMENT DATES

Payment dates for income tax

Payment	**Filing date**
First interim payment (1)	31 January in the tax year
Second interim payment (1)	31 July following the tax year end
Balancing payment	31 January following the tax year end

(1) Interim payments are not required if the tax paid by assessment for the previous year was less than:

£1,000; or

20% of the total tax liability (income tax and Class 4)

Payment dates for capital gains tax

Capital gains tax is payable by 31 January following the tax year end.

Payment dates for corporation tax	
Corporation tax	Nine months and one day after the end of an accounting period
Corporation tax by instalments – large companies	The 14th day of months 7, 10, 13 and 16 counted from the start of a 12-month accounting period
Corporation tax by instalments – very large companies	The 14th day of months 3, 6, 9 and 12 counted from the start of a 12-month accounting period

Payment dates for VAT

	Due date
Electronic payment	7 calendar days after the last day of the month following the end of the return period
Direct debit payment	Collected automatically 3 working days after electronic payment due date

MAIN PENALTY PROVISIONS

PENALTIES FOR INCORRECT RETURNS

The penalties are a percentage of the potential lost revenue

Reason for penalty	Maximum penalty	Minimum penalty with unprompted disclosure	Minimum penalty with prompted disclosure
Careless action	30%	Nil	15%
Deliberate but not concealed action	70%	20%	35%
Deliberate and concealed action	100%	30%	50%

PENALTIES FOR FAILURE TO NOTIFY

Failures to notify chargeability to tax, or liability to register for tax that leads to a loss of tax will result in a penalty. The penalties are a percentage of the potential lost revenue.

Reason for penalty	Maximum penalty	Minimum penalty with unprompted disclosure		Minimum penalty with prompted disclosure	
Deliberate and concealed action	100%		30%		50%
Deliberate but not concealed action	70%		20%		35%
		>12m	<12m	>12m	<12m
Any other case	30%	10%	Nil	20%	10%

COMPANIES: PENALTIES

Offence	Maximum Penalty
Failure to notify chargeability within 12 months of end of accounting period	See above: penalties for failure to notify

Corporation tax: penalties for late filing of a corporation tax return

Offence	Penalty(1)
Late return, up to 3 months late	£100 fixed penalty, or £500 for persistent failure
Return more than 3 months late	£200 fixed penalty, or £1,000 for persistent failure
Return filed more than 18 months but less than 24 months after end of return period	Tax geared penalty of 10% of tax unpaid 18 months after end of return period
Return filed more than 24 months after end of return period	Tax geared penalty of 20% of tax unpaid 18 months after end of return period

(1) The tax geared penalty is charged in addition to the fixed penalty but only one of each type of penalty is charged.

INDIVIDUALS: PENALTIES

Offence	Maximum Penalty
Failure to notify chargeability by 5 October following tax year end	See above: penalties for failure to notify
Late payment of income tax or capital gains tax: [1]	
Unpaid 30 days after payment due date	5% of tax unpaid
Unpaid 6 months after payment due date	Further 5% of tax unpaid
Unpaid 12 months after payment due date	Further 5% of tax unpaid

(1) Late payment penalties do not apply to payments on account.

Income tax and CGT: penalties for late filing of a self-assessment return

Offence	Maximum Penalty
Late return	Immediate £100 fixed penalty
Return more than 3 months late	Daily fixed penalties of up to £10 per day for maximum 90 days
Return more than 6 months but less than 12 months late	Further tax geared penalty of 5% of tax due (minimum £300)
Return 12 months late	Further tax geared penalties apply (minimum £300): 100% if deliberate and concealed[1] 70% if deliberate but not concealed[1] 5% in all other cases

(1) These tax geared penalties are reduced for disclosure as per penalties for incorrect returns.

PAYE: penalties for late returns/ submissions

Number of employees	Monthly penalty
1 to 9	£100
10 to 49	£200
50 to 249	£300
250 or more	£400

If the form is more than three months late, an additional penalty is due of 5% of the tax and NIC that should have been reported.

Additionally, there is a £300 penalty per late P11D return, with an extra £60 per day charged if the delay continues.

PAYE: penalties for late payment

	No of late payments	% of tax unpaid[1]
Penalties for late payment of in-year PAYE depend on the number of defaults in the tax year	1st	nil
	2nd, 3rd & 4th	1%
	5th, 6th & 7th	2%
	8th, 9th & 10th	3%
	11th or more	4%
Where a penalty has been imposed and the tax remains unpaid at 6 months		5%[2]
Where a penalty has been imposed and the tax		5%[2]

remains unpaid at 12 months

(1) The percentage penalty is applied to the total amount that is late in the relevant tax month.

(2) The 6 month and the further 12 month penalties are in addition to the initial penalty for late payment.

VAT: penalties

Offence	Maximum Penalty
Failure to notify liability for registration or change in nature of supplies by person exempted from registration	See above: penalties for failure to notify

VAT: late payment or late filing – default surcharge

Default involving late payment of VAT in the surcharge period[1]	Surcharge as a percentage of the VAT outstanding at the due date
First	2%[2]
Second	5%[2]
Third	10%[3]
Fourth	15%[3]

(1) Default if late payment of VAT or filing of VAT return and surcharge liability notice issued, but default surcharge only applies on late payment.

(2) No surcharge if it would be less than £400.

(3) Minimum £30 payable.

VAT errors

An error made on a VAT return can be corrected on the next return provided it was not deliberate and does not exceed the greater of:

- £10,000 (net under-declaration minus over-declaration); or
- 1% x net VAT turnover for return period (maximum £50,000)

Alternatively, a 'small' error which is not deliberate may be corrected via the submission of form VAT652. Errors which are not 'small' or errors which are deliberate should be notified to HMRC on form VAT652.

RECORD KEEPING PENALTY

Offence	Maximum Penalty
Failure to keep and retain tax records	£3,000 per tax year / accounting period

INCOME TAX RATES: 2020/21

	Rate	Taxable income band
Main rates		
Basic rate	20%	£1 – £37,500
Higher rate	40%	£37,501 – £150,000
Additional rate	45%	Over £150,000
Savings rates		
Starting rate for savings	0%	£1 - £5,000
Savings income nil rate	0%	First £1,000 or £500
Savings basic rate	20%	Otherwise chargeable at basic rate

	Rate	Taxable income band
Savings higher rate	40%	Otherwise chargeable at higher rate
Savings additional rate	45%	Otherwise chargeable at additional rate
Dividends rates		
Dividend nil rate	0%	First £2,000
Dividend ordinary rate	7.5%	Otherwise chargeable at basic rate
Dividend upper rate	32.5%	Otherwise chargeable at higher rate
Dividend additional rate	38.1%	Otherwise chargeable at additional rate
Default rates		
Default basic rate	20%	
Default higher rate	40%	
Default additional rate	45%	
INCOME TAX RELIEFS		**2020/21**
Personal allowance		£12,500

CGT RATES

	2020/21
Gains falling within the remaining basic rate band	10%
Gains exceeding the basic rate band	20%

CORPORATION TAX RATES

	FY 2020
Tax rate	19%
Augmented profits limit for corporation tax payment dates – large companies	£1,500,000
Augmented profits limit for corporation tax payment dates – very large companies	£20,000,000

NATIONAL INSURANCE CONTRIBUTIONS

	2020/21		
NIC CLASS 1	**Annual**	**Monthly**	**Weekly**
Primary threshold (PT)	£9,500	£792	£183
Secondary threshold (ST)	£8,788	£732	£169
Upper earnings limit (UEL)	£50,000	£4,167	£962
Apprentice upper secondary threshold (AUST) for under 25s	£50,000	£4,167	£962
Upper secondary threshold (UST) for under 21s	£50,000	£4,167	£962

NIC CLASS 1		2020/21 Annual	Monthly	Weekly
Employment allowance (per year, per employer)	£4,000			
Class 1 Primary contributions on earnings between PT & UEL	12%			
Class 1 Primary contributions on earnings above UEL	2%			
Class 1 Secondary contributions on earnings above ST where employee aged 21 or over and not an apprentice under the age of 25	13.8%			
Class 1 Secondary contributions on earnings between ST & AUST for apprentices under the age of 25	0%			
Class 1 Secondary contributions on earnings above AUST for apprentices under the age of 25	13.8%			
Class 1 Secondary contributions on earnings between ST & UST for employees under the age of 21	0%			
Class 1 Secondary contributions on earnings above UST for employees under the age of 21	13.8%			
Class 1A contributions	13.8%			

	2020/21
NIC CLASS 2	
Normal rate	£3.05 pw
Small profits threshold	£6,475 pa
NIC CLASS 4	
Annual lower profits limit (LPL)	£9,500
Annual upper profits limit (UPL)	£50,000
Percentage rate between LPL & UPL	9%
Percentage rate above UPL	2%

VAT	
Standard rate of VAT	20%
Reduced rate of VAT	5%

Syllabus Area: Income Tax & NIC

INCOME TAX RATES: 2020/21	Rate	Taxable income band
Main rates		
Basic rate	20%	£1 – £37,500
Higher rate	40%	£37,501 – £150,000
Additional rate	45%	Over £150,000
Savings rates		

INCOME TAX RATES: 2020/21	Rate	Taxable income band
Starting rate for savings	0%	£1 - £5,000
Savings income nil rate	0%	First £1,000 or £500
Savings basic rate	20%	Otherwise chargeable at basic rate
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Dividend upper rate	32.5%	Otherwise chargeable at higher rate
Dividend additional rate	38.1%	Otherwise chargeable at additional rate
Default rates		
Default basic rate	20%	
Default higher rate	40%	
Default additional rate	45%	

INCOME TAX RELIEFS	2020/21
Personal allowance(1)	£12,500
Marriage allowance(2)	£1,250

(1) The personal allowance of any individual with adjusted net income above £100,000 is reduced by £1 for every £2 of adjusted net income above the £100,000 limit.

(2) A spouse or civil partner who is a basic rate taxpayer or who has income of less than the personal allowance is allowed to transfer £1,250 of their personal allowance (ie 10% rounded up to the next £10) to their spouse/civil partner provided the recipient spouse is a basic rate taxpayer.

CAPITAL ALLOWANCES

First year allowances available

100% on new and unused zero emissions goods vehicles

100% on new and unused low emission cars ie electrically propelled or with CO_2 emissions of not more than 50 g/km

100% on electric vehicle charging points

Annual investment allowance

£200,000 pa of expenditure incurred by any business on certain plant and machinery from 1 January 2021.

Writing down allowances

18% pa in the main pool

COMPANY VANS, CARS AND FUEL

Van scale charge

No charge applies if there is insignificant private use

£2,792 if van has zero CO_2 emissions and £3,490 if it has CO_2 emissions

Additional £666 if private fuel provided for the van

Company cars – cash equivalent	
Zero emissions cars	0% of list price

Company cars – cash equivalent

Hybrid cars with emissions 1-50g/km	2% of list price for cars with a battery range of >130 miles
	5% of list price for cars with a battery range of 70-129 miles
	8% of list price for cars with a battery range of 40-69 miles
	12% of list price for cars with a battery range of 30-39 miles
	14% of list price for cars with a battery range of <30 miles
Other cars	15% of list price for cars emitting 51-54g/km
	16% of list price for cars emitting 55-59g/km
	17% of list price for cars emitting 60-64g/km
	18% of list price for cars emitting 65-69g/km
	19% of list price for cars emitting 70-74g/km
	20% of list price for cars emitting 75-79g/km
	Increased by 1% per 5g/km over the 75g/km relevant threshold

Relevant % is reduced by 2% for cars first registered from 6 April 2020

Capped at 37% of list price (ie emissions of 160g/km or more for cars first registered before 6 April 2020 and 170g/km for cars first registered from 6 April 2020)

Diesel cars that meet the Real Driving Emissions Step 2 (RDE2) standard are treated as above, all other diesel cars have a 4% supplement added to the relevant percentage (subject to 37% cap)

Private fuel provided for company car

£24,500 x company car %

PAYE CODES

L	tax code with personal allowance
M	tax code with personal allowance plus claiming marriage allowance
N	tax code with personal allowance less surrendered marriage allowance
S	income taxed at Scottish rate of income tax
C	income taxed at Welsh rate of income tax
K	total allowances are less than total deductions
T	tax code includes other calculations to work the personal allowance, for example it has been reduced because estimated annual income is more than £100,000

NATIONAL INSURANCE CONTRIBUTIONS

	2020/21		
NIC CLASS 1 CONTRIBUTIONS	**Annual**	**Monthly**	**Weekly**
Primary threshold (PT)	£9,500	£792	£183
Secondary threshold (ST)	£8,788	£732	£169
Upper earnings limit (UEL)	£50,000	£4,167	£962

NIC CLASS 1 CONTRIBUTIONS		2020/21 Annual	2020/21 Monthly	2020/21 Weekly
Apprentice upper secondary threshold (AUST) for under 25s		£50,000	£4,167	£962
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	2020/21
NIC CLASS 2 CONTRIBUTIONS	
Normal rate	£3.05 pw
Small profits threshold	£6,475 pa
NIC CLASS 4 CONTRIBUTIONS	
Annual lower profits limit (LPL)	£9,500
Annual upper profits limit (UPL)	£50,000
Percentage rate between LPL & UPL	9%
Percentage rate above UPL	2%

Syllabus area: Capital Gains

	2020/21
Annual exempt amount	£12,300
Gains falling within the remaining basic rate band	10%
Gains exceeding the basic rate band	20%
Basic rate band	£1 – £37,500

Syllabus area: Corporation tax

	FY 2020
Tax rate	19%
Augmented profits limit for corporation tax payment dates – large companies	£1,500,000
Augmented profits limit for corporation tax payment dates – very large companies	£20,000,000

CAPITAL ALLOWANCES

First year allowances available

100% on new and unused zero emissions goods vehicles

100% on new and unused low emission cars ie electrically propelled or with CO_2 emissions of not more than 50 g/km

100% on electric vehicle charging points

Annual investment allowance

£200,000 pa of expenditure incurred by any business on certain plant and machinery from 1 January 2021.

Writing down allowances

18% pa in the main pool

PAYMENT DATES

Payment dates for corporation tax	
Corporation tax	Nine months and one day after the end of an accounting period
Corporation tax by instalments – large companies	The 14th day of months 7, 10, 13 and 16 counted from the start of a 12-month accounting period
Corporation tax by instalments – very large companies	The 14th day of months 3, 6, 9 and 12 counted from the start of a 12-month accounting period

Syllabus area: Value Added Tax

VAT		
Standard rate		20%
Reduced rate		5%
Annual registration limit	From 1 April 2017	£85,000
Deregistration limit	From 1 April 2017	£83,000
VAT fraction (standard rated)		1/6

Cash accounting	**£**
Turnover threshold to join scheme	1,350,000
Turnover threshold to leave scheme	1,600,000
Annual accounting	
Turnover threshold to join scheme	1,350,000
Turnover threshold to leave scheme	1,600,000

Flat rate scheme	
Annual taxable turnover limit (excluding VAT) to join scheme	150,000
Annual total income (including VAT) to leave scheme	230,000

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